**Market Forces**

We often hear politicians and others say that there should be no control of prices and that prices should be left to “Market Forces”. But what does this mean? Perhaps the best way to explain this is to set up what in Economics are called models.

 Models are simplified versions of the real world. In Economics because we deal with people and as a result cannot conduct experiments as the scientist might do we need to reduce what happens to the simplest possible level. Economists simplify situations by making assumptions. The most common assumption Economists make is that people are rational. That means that people use their common sense and for example would not pay more for a good when they could buy one exactly the same for a cheaper price next door.

This idea is best explained by an example. Let us set up a model with the following assumptions:

1. Everyone owns a DVD Player
2. Everyone likes all kinds of movies and could obtain as many as they could afford at the prices offered.
3. Everyone gets pocket money of $20.00 per week.
4. Everyone is rational.

Complete the following table:

|  |  |
| --- | --- |
| Price of DVDs | Quantity you are willing and able to buy(Given the assumptions above) |

$1

$2

$3
$4

$5

$6

$7

$8

$9

$10

$11

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What you have constructed is called an individual demand schedule. In the space below construct a graph with the price on the vertical axis and the quantity will to be purchased on the horizontal axis.

Now find five friends and record their demand for DVDs.

Copy their demand schedules and add them up so that you get what is called a market demand schedule.

You should find that when you graph this schedule you get a smoother demand curve.

**Demand**

Demand can be defined as the quantity of a good or service that consumers are willing and able to buy at various prices at a particular time. Demand is shown on the demand curve diagram. As can be seen from the diagram, when the price gets higher the quantity demanded gets smaller. Another way of saying this is that the demand curve slopes downwards to the right. Draw the market demand curve for DVD movies here:

Price

 Quantity Demanded

What do you think would happen to the Demand Curve if everyone started getting $40 per week pocket money? Draw the old and the new demand curves below. (There is no need to draw these curves to scale as it is the change or what economists call the shift in the demand curve that is important.)

Price

 Quantity Demanded

Can you think of any other changes which would cause the demand curve to shift?

**Worksheet on Demand**

1) The demand for ice-cream cones in a small country town is as follows:

Price Quantity Demanded

50c 500

$1.00 400

$1.50 300

$2.00 200

$2.50 100

$3.00 50

Draw the demand curve to scale on graph paper. What would happen to the demand curve if the weather became very cold? Show this change on the graph and explain what has happened.

2) Below you will find demand schedules for three different goods (Goods A, B& C). Draw demand curves to illustrate the demand for each good making sure you use the same scale each time.

 Good A Good B Good C

Price Qty Demanded Price Qty Demanded Price Qty Demanded

$1 160 $1 120 $1 200

$2 80 $2 110 $2 80

$3 50 $3 90 $3 30

$4 40 $4 80 $4 15

$5 30 $5 70 $5 10

a) Describe the difference between the shapes of the curves for each of these products.

b) Which one do you think is more likely to be a necessity? Why do you say this?

c) Which one do you think is more likely to be a luxury? Why?

d) Do you think the demand curve for petrol appears here? Which one? If not, why not?

3) The demand for backyard swimming pools has increased greatly over the last 40 years. Can you explain the reasons for this? Draw diagrams to illustrate what has happened.

**Supply**

Supply can be defined as the quantity of a good or service that producers are willing and able to sell at particular prices at a particular time. To understand supply we can set up a model with the following assumptions:

1. Everyone owns their own home.
2. Everyone is rational.
3. Everyone house is more or less the same.

Construct a Supply Schedule for houses in the area and then draw the supply curve.

Price Quantity

 Price

 Quantity

Notice what happens to the supply as the price rises. The supply curve slopes ……………………… to the right. The reason for this is that as the price rises more people are willing to supply their houses (i.e. they are more willing to put them on the market.) What is happening is that stock is being converted into supply. In other words as the price rises more people are willing to sell their houses.

Although houses are a good example to explain the fact that supply curves slope upwards to the right they are not like many goods and services in that they last a long time and take a long time to build.

Can you think of any reasons why the supply curve might shift?

Consider the supply of shirts. What factors do you think will affect their supply?

What about hamburgers?

Try to make a general list of the factors which will affect the supply of most goods and services.

**Worksheet on Supply**

1) The supply of lawnmowers in a city is shown by the following schedule:

Price Quantity Supplied

$100 50

$200 200

$300 500

$400 1000

$500 1500

Draw the supply curve for lawnmowers. What would happen if there were a technological breakthrough, which made lawnmowers cheaper to make? Draw the new supply curve.

Applied Supply and Demand Analysis

a) Consider the market for TV sets. Draw a diagram and explain what affect the following changes will have on the TV set market.

1. Movie theatres offer very cheap tickets.
2. A change in technology makes TVs cheaper to make.
3. All free to air TV channels close down.
4. There is a successful advertising campaign which results in many more people becoming involved in outdoor sport.
5. The size of the population increases by 10%.
6. The average income of people rises by 20%.

Remember for each question you should start with a diagram showing the supply and demand for TVs.

b) Consider the market for tomatoes. Draw a diagram and explain what affect the following changes will have on the market for tomatoes.

1. There is a plague of caterpillars which damages most of the tomato crop.
2. A new type of breed of tomato is developed. This new type produces twice as many tomatoes as the old type of plant.
3. There is a long period of warm weather which encourages people to eat more salads.
4. There are worries over the insecticides used to control bugs which attack tomatoes.